RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

Since 1958 •

Post Office Box 1759, La Jolla, California 92038

26 Letters Per Year • $250 annually

June 19, 1996 **LETTER 1202**

THE PICTURE: The June 5 *WSJ* carried an article entitled, "Short Sellers Face a Bubble That Won't Burst." The article then proceeds to detail the disasters that have befallen a number of well-known professional short-sellers.

The short-sellers should have been watching my **Primary Trend Index.** To sell short while the PTI continues to go to consecutive new highs amounts to financial suicide. As I've said so many times before, you're free to stand aside, to disbelieve or ignore the PTI -- but *don't ever bet against it.* And a short sale while the PTI is hitting new highs is definitely a bet against it.

Referring to the chart of the D-J Averages below, the number one question for the market is -- will the Dow be able to better its bull market high of **5778.00**? And will the Transportation Average be able to better its corresponding bull market high of **2296.20**? And finally, will the S&P 500 be able to better its own record high of **678.51**? The *longer the elapsed time* without new highs, the more suspicious we can be that the market is (finally) running into trouble.

Talk is cheap in this industry, and predictions are, at best, interesting. But let's face it -- you can always hear "expert" predictions from either the bull side or the bear side. But if you deal in **reality**, I suggest that you watch the Averages. Veteran market watchers do exactly that -- while treating all forecasts, bull and bear, with the proverbial grain of salt.

MOOD SWINGS: Everybody on Wall Street seems to be trying to explain "why the stock market is so high," why there is "so much speculation," why each day brings out a new mutual fund, and why so many people (who have never owned a stock before) have belatedly rushed into the market.

Back at the turn of the century Charles H. Dow gave us the answers, but not one out of a hundred investors has ever taken the trouble to read what Dow actually said. This is the 100th anniversary of the first D-J Average, and in view of this, I thought this would be a good time to consult the old master.

So last week I pulled out my tattered copy of "The ABC of Stock Speculation," a little volume which contains 20 of Charles Dow's original *Wall Street Journal* editorials. Believe me, these are wise words, words worth heeding.

Here is some of what Dow said: *"The business community has a tendency to go from one extreme to the other. As a whole, it is either contracting business under a belief that prices will be lower, or expanding under a belief that prices will be higher. It appears to take ordinarily five to six years for public confidence to go from the point of too little hope to the point of too much confidence, and then five or six years more to get back to the condition of hopelessness."*

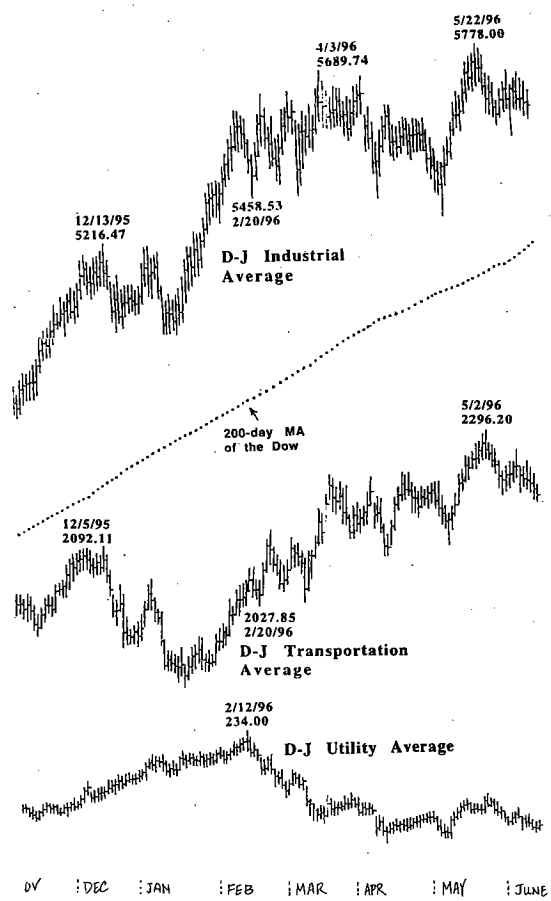
In one of his most famous statements, Dow noted,*"There is always a disposition in people's minds to think the existing conditions will be permanent. When the market is down and dull, it is hard to make people believe that this is the prelude to a period of activity and advance. When prices are up and the country is prosperous, it is always said that while preceding booms have not lasted, there are circumstances connected with this one which make it unlike its predecessors and give assurance of permanency. The one fact pertaining to all conditions is that they will change."*

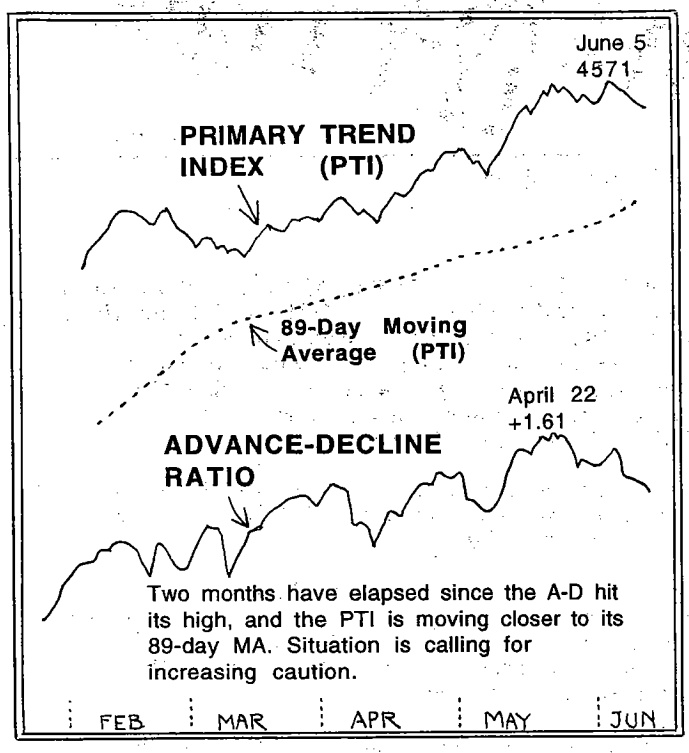
June 7 DJIA 5697.11; PTI 4567; A-D Ratio +0.86
June 14 DJIA 5649.45; PTI 4550; A-D Ratio +0.52
Dow Yield: 2.19%; Dow Price/Earnings: 18.1
Dow 200-day MA: 5244; Dow 30-day MA: 5639
Dow Times Book Value: 4.22; PTI 89-day MA: 4505
Percentage of Undervalued Blue-chips: 2%!
Gold 200-day MA: 393.07; Gold-PTI: 570

In another editorial Dow writes, *"It is impossible to tell in advance the length of any primary movement, but the further it goes, the greater the reaction when it comes."*

Dow was not only a student of the markets, he was a student of human nature. And he was well aware of the cycle of human nature, the tendency of people to go from an extreme of hope and confidence to the opposite extreme of despair and disillusionment -- and then back to optimism again.

I've seen these cycle swings many times in my lifetime, and at each extreme it seems to me almost grotesque that so much is forgotten by so many normally clear-thinking people. For instance, now, as I write this, I don't think anyone can envision or is even thinking in terms of a major, crushing bear market. Few investors today can even imagine a series of events (political, social and economic) that will bring out such comments as "this has got to be the end of the US economy and the free enterprise system, as we know it," or "if anyone ever mentions common stocks to me again, I swear I'll strangle them."





Sound far-fetched? Sound totally implausible? I promise you that somewhere in the next one, two or five years we will be hearing this kind of anguished comment again. How can I promise something that has not yet occurred and "maybe never will"? I can predict those remarks on the basis of repetitive mood swings going back throughout human history.

In an editorial Dow notes that *"commercial crises occurred during 1701, 1712, 1731-32, 1742, 1752, 1772-3, 1783, 1793, 1805, 1815, 1825, 1836, 1847, 1857, 1866, 1878, 1884, and 1893."*

Ah, you say, but today we have the Fed, whose action will mitigate any crisis. Won't the Fed always fight recession and won't the Fed do whatever it takes to restore equanimity (as it did in 1987 and again in 1990)?

My answer is that the Fed can feed the fires of prosperity and inflation during a bull market, but in a true primary bear market the Fed will be helpless to turn the tide.

All this notwithstanding, as I write this the primary trend of the market continues bullish. So why deal with events that have not yet materialized? Why indeed.

INVESTMENT POSITION: Who needs Vegas, we've got the stock market. Now consider this: (1) This market features the highest price-to-book ratio in Wall Street history. (2) This market has the lowest dividend yield in history. (3) This is the oldest primary bull market in history. (4) This market has had the longest rise in history without a 10% correction.

Here's something else to consider: The broad S&P 500 hit a record high of 661.45 on February 12. Four months later or last week, (June 17) the S&P 500 was at 665.48, only a fraction higher, following four months of huge volume. Let me put it this way -- somebody is supplying eager buyers with a lot of stock.

Personally, I'm satisfied to watch the show. And as I said, a lot of somebodies are supplying the market with a lot of stock. I tend to share the philosophy of the unknown somebodies.

By the way, the exit of Jeff Vinik from the Magellan Fund, I thought, was very significant. It tells us that if you're a fund manager, if you even think about being defensive, you can look for another job. So forget there's such a thing as a T-bill or a bond. Brother, you buy stocks as the cash comes in, and you keep up with the S&P or else. Yeah, this is a mania all right. And it will end in only one way -- exhaustion.

CRITICAL STUDIES & COMMENTS. By the way, I consider the following piece the most important that I have written this year. Please study it carefully.

Manias: The *McAlvany Intelligence Advisor* (PO Box 84904, Phoenix, AZ 85071) lists nine historic manias. These manias are identified by frenzied crowd participation and massive rises in the various items. The question, of course, is whether the current bull market has reached the point where it can be characterized as a major mania. Taking the bull market as having started at Dow 577 in 1974, the Dow has now risen to 5778, a rise of 901%. In terms of percentage of advance, in terms of crowd participation and in terms of intensity of speculation, the stock market of the '90s can certainly (in my opinion) be classified as **one of the great historic manias.**

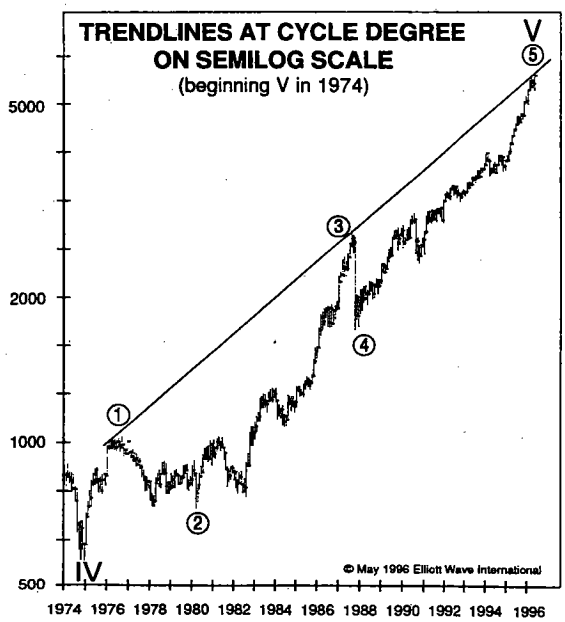
MANIAS IN HISTORY

	% Rise	Length Months	% Decline	Length Months
TULIP MANIA BUBBLE Holland 1634-37	5900%	36	-93%	10
MISSISSIPPI SHARES France 1719-20	6200%	13	-99%	13
SOUTH SEAS SHARES Britain 1719-20	1000%	8	-84%	6
AMERICAN STOCKS USA 1921-29	497%	95	-87%	33
MEXICAN STOCKS Mexico 1978-81	785%	30	-73%	18
SILVER USA 1979-82	710%	12	-88%	24
HONG KONG STOCKS Hong Kong 1970-74	1200%	28	-92%	20
TAIWAN STOCKS Taiwan 1986-90	1168%	40	-80%	12
JAPANESE STOCKS Japan 1965-?	3720%	288	so far -55%	36
AMERICAN STOCKS USA 1982-?	728%	so far 175	????	?

COURTESY: The McAlvany Intelligence Advisor
P.O. Box 84904, Phoenix, AZ 85071

Note that the aftermath of previous manias was painful, to say the least. Of the nine previous-listed manias, seven resulted in losses of 80% or more of the total preceding gains. If nothing else, the above should provide food for thought -- and caution.

Trendline: Bob Precther, in his always fascinating *Elliot Wave Theorist* (PO Box 618, Gainesville, GA 30503), notes that the Dow has hit its upper trendline on *both* arithmetic and semilog scale. This is action that is seldom seen. The fact that the Dow is pressing against its upper trendline suggests tremendous resistance at around the 5700 level of the Dow. **Russell comment:** What does it mean if the Dow advances above the upper trendline? In my experience, when the price action surges to, and then above, the upper trendline, the item has reached the "blow-off" stage and such extreme surges are generally short-lived. However, the fact is that the Dow has **not yet bettered its upper trendline** and it now seems to be encountering strong upside resistance (chart of the Dow below courtesy of *Elliott Wave Theorist*).



Sharply divided opinions exist regarding what will happen when the next bear market materializes. Prechter in his latest report makes an excellent case for deflation. His report takes a decidedly cynical view of the newly announced inflation-adjusted long-term US government bonds. Since the government is almost always wrong on its timing, the fact that the government will be offering inflation-adjusted bonds suggests that the danger ahead lies not with inflation but with deflation. Also, at a recent seminar Prechter reports that 88% of the professionals predicted a rise in inflation over the next 12 months (room for contrary opinion?).

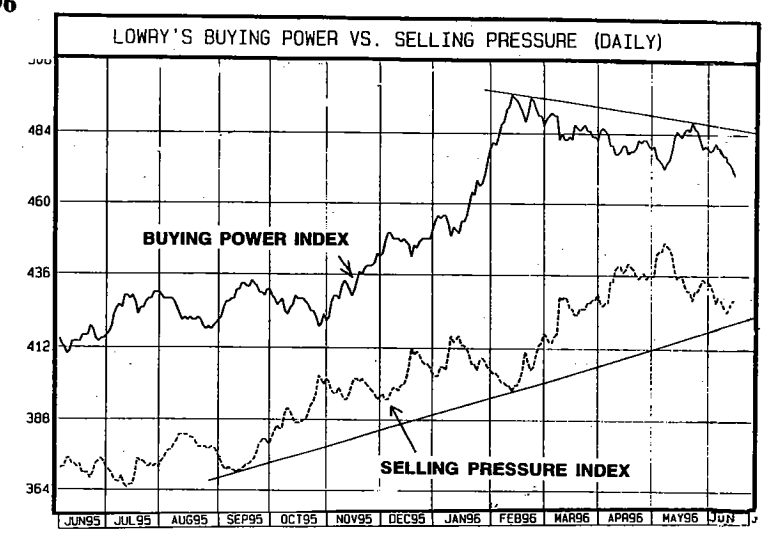
Russell comment: It's obvious that if the economic and stock market cycles turn down, the Fed will do everything in its power to re-inflate both the economy and the markets (the Fed has done this numerous times, as per post-1987 and as per the re-liquefaction of the banks during the '90s). However, it's been two decades since the Fed has had to deal with a primary bear market. The last true bear market occurred back in 1973-74, at which time things were very different and the Dow was in the 550-1000 area.

If we experience a primary bear market from the current or even higher levels, the losses could be staggering. Personally, I don't believe the Fed will be able to neutralize the primary bear forces during the next bear market. Therefore, in the next bear market I foresee *deflation,* the phenomenon that few people are prepared for or even thinking about.

Lowry's: I've been following the excellent *Lowry's* service since the 1960s, and their reports are particularly significant now. *Lowry's* is based on their proprietary Buying Power and Selling Pressure indices. These indices have been computed in real times since the late '30s (the Buying Power and Selling Pressure indices are moving averages based on stocks moving up or down and their volume). Note on the chart that the stock market started to attract **rising Selling Pressure** in September of 1995. Nobody knows who's doing the selling, it doesn't matter, but the important point is that this market HAS BEEN ATTRACTING INCREASING SELLING (note the rising trendline under Selling Pressure). I want to stress this again -- trend Selling Pressure is coming into this market.

Once a market attracts Selling Pressure on a trend basis, that selling usually increases until at some undetermined point ahead, Selling Pressure finally overpowers Buying Power. When that happens, the result is usually either a major correction or a bear market.

Now note that **Buying Power peaked in mid-February.** Once Buying Power peaks in the face of rising Selling Pressure, there is usually a period of around *four to six months* before the



two indices actually cross. My guess is that we could get a crossing sometime during the next two to four months.

For this reason, I expect the stock market to top out *this year.* A major top-out before November 1996 would be a shocker, since a top-out before the presidential election would present a situation that neither the political parties nor investors are prepared for [*Lowry's Reports,* (407) 842-3514].

Of course, a confirmation of a top would have to include deterioration and then a bear signal on the part of my Primary Trend Index. It seems to me that 1996 is setting up as a very fascinating year.

Volatility: I've written about the stock market's low volatility before, but *Growth Fund Guide* (Box 6600, Rapid City, SD 57709) has just published some very interesting comments on the subject. In the whole history of the Dow, its *average* annual daily closing high to daily closing low has been -17.0%. But over the past five years the Dow's annual high-to-low span was a mere 6.4%. And last year, 1995, we witnessed the smallest high-to-low swing in history, an incredibly low 3.3%. The largest five year high-to-low average swings occurred during the 1929-33 period, -46.6%.

Russell Comment: Somewhere ahead the market will do what it has to -- to bring annual volatility back close to its 100-year average of -17.0%. Therefore, expect BIG action (volatility) in the years ahead, maybe starting later this year or in 1997. "After the calm comes the storm."

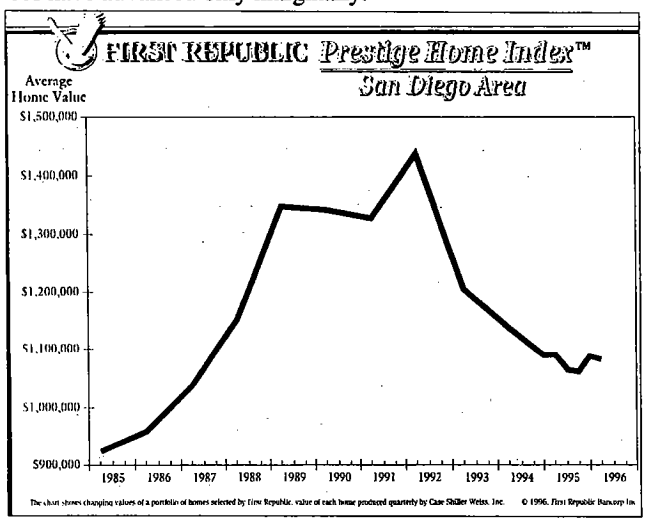
NOTES & QUOTES: You like contrary opinions, then try this one. Richard Hokenson, chief economist for Donaldson, Lufkin & Jenrette Securities, forecasts a brief but fierce recession in '97, one that will generate real price deflation for the first time since the '50s. As a result, he sees interest rates dropping a shocking 3% and the Dow diving below 4000. What would set off all this trouble? Hokenson sees a big drop-off in household formation, leading to a sharp decline in demand for goods. He sees falling demand for consumer durables, which will reduce the total output of goods and services by 2.7% between December '96 and the end of '97. **Russell comment:** If Hokenson is right, the real play coming up would be bonds. Personally, I'll start to believe this scenario if the September bond contract breaks out above 110. Ain't happening yet.

* *

What's happened to luxury home prices? Five years ago I drove through Beverly Hills with a friend who was shopping for a home. Every house we looked at was priced at over a million dollars, most in multiples of a million. I said to myself, "Something's crazy. According to these prices, literally everyone living in Beverly Hills is a multi-millionaire. Everybody here owns a house worth $2 to $3 to $4 million. My only reasonable conclusion is that these prices are too damn high." In mid-1992 the price of housing

started to crumble. By '95 many of these houses were selling at anywhere from one-third to a half below their peak prices. The housing market had returned to some kind of reality. Of course, at the same time the stock market started moving into its own brand of fantasy land. As this is written, my opinion is that the stock market, in terms of valuations, is where the California housing market was in 1991. And for the first time in modern memory the value of consumers' stock portfolios has surpassed the total value of their homes. America's "savings" are now in equities, not in their homes.

This chart (courtesy First Republic Bancorp) shows the dollar value of the average "prestige home" in San Diego. Said an executive of First Republic, "San Diego luxury home values are at their lowest price since March, 1988." Recently, however, sales have picked up. Said another executive last week, "Sales are phenomenal. More sales were generated in the first month of this year than last year's entire first quarter." Sales have picked up but prices have advanced only marginally.



The *International Herald Tribune* ran a comparative cost study of home affordability in various world cities. Interestingly, London has both the highest salaries and the highest house prices. In Paris housing is expensive and hard to find. In Madrid salaries are low but home prices are almost as expensive as Paris. Conclusion: San Francisco and Sydney are "the best bets" for living a comfortable life. "High property prices are the rule in Asia, but Hong Kong, Singapore and Tokyo offer the consolation of comfortable salaries."

CITY	SALARY	PROPERTY PURCHASE	
		Cost	x Year's Salary
Bombay	$20,000	$231,000	11.55
Düsseldorf	$200,000	$670,000	3.35
Hong Kong	$260,000	$1,900,000	7.3
London	$225,000	$900,000	4
Madrid	$66,000	$500,000	7.5
New York	$225,000	$600,000	2.6
Paris	$162,318	$608,695	3.75
San Francisco	$200,000	$300,000	1.5
Singapore	$149,514	$984,474	6.6
Sidney	$149,514	$373,785	2.5
Tokyo	$295,000	$900,000	3.05

All figures shown are in U.S. dollars

* *

Whether you're pro-abortion or against it is your business. But if you're a staunch Republican, you've got problems. I read just about all the women magazines, and I'm well aware of women's sentiments. Here's the cap from an article in the July *Mademoiselle*. The women's vote (particularly single women) is going to swing the election, so you might send this page to your local GOP Congressman or Senator.

Warning to the Republican party: Listen to women–or lose

IN 1992 I WAS A BUSH delegate to the Republican National Convention in Houston. Disgusted because the convention had been taken over by antichoice zealots and George Bush was going along, I turned in my credentials and walked out.

Will 1996 see another elec-

The GOP has ignored its pro-choice majority for too long. Will it happen again this year?

That struggle could produce a change thousands of Republicans have been waiting for since 1980, the year the party adopted the antichoice plank, dropped 40 years of support for the Equal Rights Amend-

ment of a strict separation of church and state. If the GOP

* *

Friends ask me why I avoid traveling. I avoid traveling because to be a traveler today (unless you've got your own plane) you've got to be a confirmed masochist. Roads are jammed, hotels are expensive, resorts are crowded and planes are late, and if they're on time, the flight is canceled. This clip from the June 6 *NY Times* states that mental stress is more dangerous to hearts than physical stress. I've known this for a long time. Which is why I avoid travel. Besides, why travel when I live in arguably the single best spot on earth (and yes, I know about Tahiti and Monaco and Hawaii).

Mental Stress Seen as the Major Heart Problem

CHICAGO, June 5 (AP) — Reactions to mental stress may be a much better indicator of who will suffer heart problems than reactions to physical stress, like running on a treadmill, a new study suggests.

The study by the Duke University Medical Center, published today in The Journal of the American Medi-

A cardiac event was defined as a heart attack, progressive chest pain or pain requiring an operation like angioplasty or bypass surgery or death.

The study of 126 people for five years showed that 27 percent of the patients who responded adversely to mental stress testing, which could

ty to pump blood from its main chamber, there was an 8 percent increase in risk of suffering a cardiac event, Dr. Blumenthal said. An electrocardiogram does not measure the heart's ability to pump blood.

The study suggests that mental stress tests might identify far more patients at risk for heart attacks

* *

Sir John Templeton, founder of the Templeton group of funds, has been a bull for what seems like centuries. Therefore, I was surprised to see this quote: *"Bear markets start at the point of maximum optimism and bull markets start at the point of maximum pessimism. We are close to maximum optimism. There is an arrogant belief that things are going to go this way indefinitely."* (From the excellent *Aden Forecast*, PO Box 66710, St. Louis, MO 63166.)

* *

A significant comment regarding Warren Buffett's recent sale of 350,000 shares of the Baby Berkshires: "Nobody ever made money betting against Warren Buffett". And in case you didn't notice, Buffett is selling shares in Berkshire, not buying 'em back.

* *

Talk about selling, Garth Brooks has sold 60 million albums, passing Billy Joel as the best-selling solo musical artist in history (who says country & western isn't HUGE).

* *

My wife, Faye, is on a five-day business trip to a town outside of Munich, Germany. She called this morning, and it sounded as if she was next door. I asked her how her hotel and surroundings were. She said it's different than the US. "How so?" I asked. "It's clean, very, very clean," was her answer. Which brings up the question, why are so many US cities so darn filthy? It's as if Americans just don't take pride in their cities. US freeways and streets are always littered with trash. It's a shame.

* *

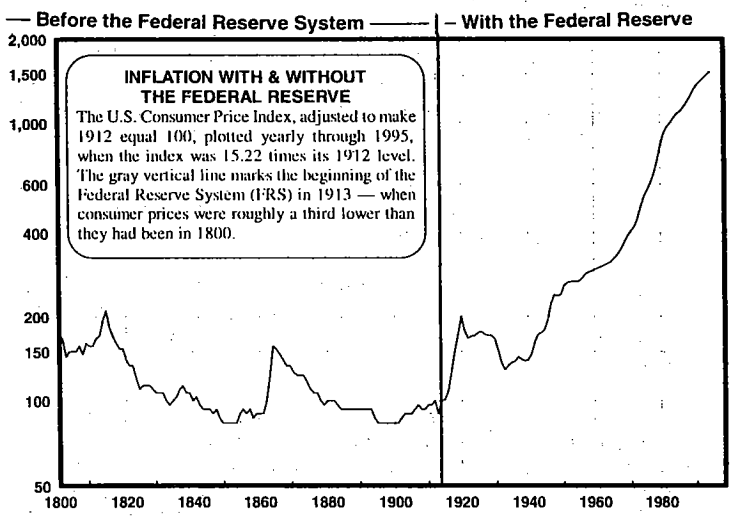
In 1992 Clintonites were enamored of the German system of generous government retirement programs, worker training programs and nationalized health care. The German system is starting to unravel. It's just too expensive. And the results are coming in. Unemployment up to 10.4%, and GDP is stagnant (actually down in the latest quarter). Also German deficits are rising to the point where EU headquarters issued a warning. When a company hires a German worker, it has to pay wage benefits equal to 85% of salary, bringing total costs to a whopping $27 an hour. German industry's response -- hire as few people as possible and move plants overseas wherever possible. The Clintonites tried to fashion the US medical plan after the German plan -- Americans didn't want any part of it. Wise choice.

* *

The Federal Reserve is often called "an engine of inflation." Any truth in this? When the US was on the gold standard, prices were

fairly stable. In those days, every dollar had to be backed by gold, and the only way the money supply could be expanded was either through a rise in the price of gold -- or if the nation accumulated more gold. Gold could be accumulated either by mining it, or by bringing it in from other nations as the US boosted its exports and called in gold from other nations. One of the basic concepts of the (unconstitutional) Federal Reserve System was that the Fed could exert some influence over the money supply.

The US Constitution specifically forbids the government to issue paper (fiat) money. But Congress circumvented that when they approved the Supreme Court's conclusion (arrived at by unbelievably circuitous reasoning) that the Fed was legal. So how has the nation fared under the Fed? This chart tells the shameful story (chart courtesy of *Harry Browne's Special Reports,* Box 5586, Austin, TX 78763).


— Before the Federal Reserve System ——— | – With the Federal Reserve
2,000
1,500
1,000
600
400
200
150
100
50
INFLATION WITH & WITHOUT THE FEDERAL RESERVE
The U.S. Consumer Price Index, adjusted to make 1912 equal 100, plotted yearly through 1995, when the index was 15.22 times its 1912 level. The gray vertical line marks the beginning of the Federal Reserve System (FRS) in 1913 — when consumer prices were roughly a third lower than they had been in 1800.
1800
1820
1840
1860
1880
1900
1920
1940
1960
1980

* *

Sports-flation: A Chicago outfit puts out what it calls the Fan Cost Index. They compute what it costs a family of four to attend a baseball game, which includes parking, popcorn and entrance fees. Lowest total is the Cincinnati Reds at $81.31. Average of all teams is $102.58. Highest is the Mets at $114.80. Gad, I remember when four of us could see a Broadway show, matinee, for $4.40 (that's right, tickets in the balcony were $1.10 a piece).

* *

The enormity of the Social Security scheme is finally beginning to dawn on Americans. With the payroll tax now at an outrageous 15.3%, this tax will have to double or the SS benefits will have to be reduced or the government will have to print the bucks to pay off tomorrow's retirees. So far, all the SS tax money goes into the current government budget, which is why the federal deficit figures are so phony. The government then puts non-negotiable IOUs in the SS trust funds. Ultimately, I think they'll have to let citizens out of SS, freeing them to whip up their own retirement plans. What about the people who are due to retire? They'll be paid with dollars, but what those dollars will buy, that's another question.

* *

I get both cable and satellite TV, and they both keep adding new channels. I like A&E's biography, and now I hear they are going to have a new channel which just shows biographies. Bravo is a fine channel (excellent jazz documentaries), I like the History channel as well as Discovery. (I'm a big fan of those wild animal shows.) Now I get the new Sundance channel. Great, we finally have a channel which shows many of the previously unobtainable documentary, experimental and amateur films. I know quite a few people who won't have a TV set in the house. They claim TV is pabulum for the mind. They're dead wrong.

* *

If there is a single guru in the world of economics today it is George Soros, he of the billion dollar profit in the British pound. The latest prediction from Mr. Soros is that there is a good chance of a single European currency by January 1999. It's basically a "political decision," he said, and many of the participants will have to work hard to meet the stringent criteria (unless, of course, the criteria are changed). He said the currencies of Germany, France, Luxembourg, the Netherlands and Austria would be the founding members plus probably Belgium.

* *

As reported by the *Financial Times*, "Bob Dole has spent a lifetime opposing other people's tax cuts. If you remember, Newt called Dole "the tax collector for the welfare state." Now the big question -- will Dole have the political guts to come out with a plan to totally change the abominable US tax situation? **Russell comment:** I've said all along that the only thing all Americans agree on is that the current tax situation is intolerable. My feeling is that Dole should denounce the current tax system and come out for a flat tax. His job will be to educate the US public to the advantages of the flat tax. If he can't do that, he'll lose (unless, of course, the American people finally come to believe that Clinton's character makes him unfit to be President).

THREE ANNOUNCEMENTS: (1) CHART BOOKS: Don't ask me why but in an industry that involves trillions of dollars, nobody else does this. What I'm talking about is chart books of the **D-J Averages** and the all-important **breadth index** (i.e. advance-decline ratio). I've been offering these chart albums for decades, and I feel they're invaluable. Actually, I started these chart-albums back in the '60s because I needed the data myself. The first volume is a *complete history* of the D-J Averages (all three Averages plus bonds and volume) going back to **1885**. Important economic and world events are notated on each page. The charts are packed in a big three-ring, hard-cover binder, one page for each year. The album is yours for $135; we pay the postage in the states. The second album covers the Dow and the extremely important A-D ratio (daily) going back to 1931. Comments regarding the action are included in many of the pages (one page for each year). The price is $95, we pay US postage. **For those who own the chart books**, the new 1995 pages are ready, price is $5 for the page of the Averages and $5 for the new A-D ratio page. Please send your money in now (outside the states there's an extra postage charge of $35 for each album). Write to Dow Theory Letters, PO Box 1759, La Jolla CA 92038.

(2) PAST LETTERS: You may be wondering what I've been doing the last 38 years. Answer: writing Dow Theory Letters. Many subscribers have asked me whether there's any way they can obtain all my past Letters. Answer: there is, I offer all my Letters, numbers 1 to 1200. They are all on Microfiche film, and I offer the complete Microfiche set for $795 postpaid. These Letters deal not only with the market but with the events of the day -- plus the usual Russell comments. To read Microfiche you will need a Microfiche reader (almost every public library has one, or you can buy your own reader). Write to Dow Theory Letters, PO Box 1759, La Jolla CA 92038.

(3) NEW BUSINESS: I've mentioned before that I have (after four decades of writing Dow Theory Letters) started a new business. The new business is just one year old, and it's been doing very well -- and many subscribers have joined. However there's a stricture -- it's now open only to participants who have total assets of at least $1 million (and this may include the value of your home). If you qualify and you'd like information on my new business, write and let me know, and I'll send you the info. No pesky pressure, no phone calls, no one to bother you. All you get is information. If you're interested, write to **Richard Russell, PO Box 229, La Jolla, CA 92038.**

* *

Last week Max Factor died. Max started life as the son of a Russian immigrant. He learned his trade in his father's store, Max Factor's Antiseptic Hair Store. Max worked often as an extra in Hollywood movies, and one of his jobs was to bring wigs back to dad's shop after each day's filming. The shop moved on to greasepaint and makeup, and when Max took over he started national advertising, particularly with his Tru-Color smudgeproof lipstick.

I have fond memories of Max Factor. My first job at the age of 16 was packing and loading trucks with Max Factor products. I had

spent about a month in 1940 looking for a job, any kind of job. Then a high school friend, Andy Rohman, called and said that he was working at a company in Harlem, and miracle, the company had an opening for loading trucks at the fat price of $18.75 a week, five days and half-days Saturday. I rushed up to the G. W. Button Co. and applied. The boss told me that yes, there was an opening, but first I had to join the union. I forget what the fee was, but I joined, and lo and behold, I had actually found a job during the Depression. I was thrilled; here I was loading trucks for better than three bucks a day. I couldn't wait to tell my parents. Richard Russell had found a job -- he was working.

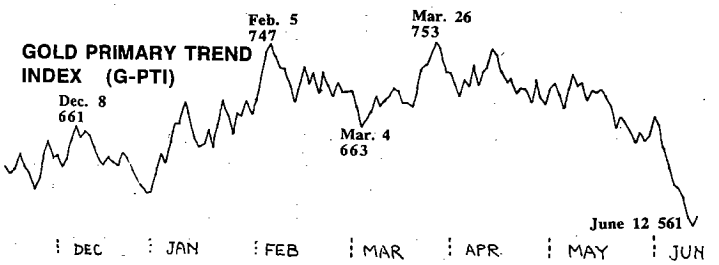
GOLD is not presenting a happy picture, and there's only one consolation, and that is that my Gold-Primary Trend Index (G-PTI) has been accurately telling the story all along. The story is this: from its March 26 high, the G-PTI has been steadily falling. On June 12 the G-PTI broke to a three-year low of 561.

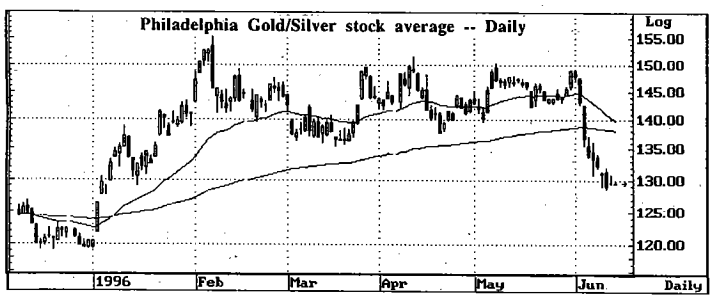
This is discouraging for gold-philes. And you have to wonder, despite everything you hear, could gold be discounting deflation ahead? Or is gold forecasting some kind of coming financial squeeze? Or is gold discounting a situation where people will be selling the metal (as the central banks have been doing) to raise cash?

The G-PTI doesn't tell us, "Why?" The G-PTI remorselessly traces the forces of supply and demand in gold and gold-oriented items, and the grim fact is that ever since March 26 supply has been overpowering demand.

The daily chart of XAU, the Phila. Gold/Silver stock average, doesn't present a pleasant picture. The XAU has broken below its March low, and it's now back to its January levels. The shorter 34-day moving average has turned down and is heading towards the longer 144-day moving average. If the 34-day MA breaks below the 144-day MA that will be a bearish indication, and it would mean that there will be tremendous resistance to pushing back above the 135-140 zone on the XAU.

I read a slew of gold reports, and most believe that gold is now basing, preparatory to a major advance or even a new bull market. That may be true, but I would want to see confirmation of that thesis in the technical picture. So far, with my G-PTI at a multi-year low and with the XAU back to its January low, the "basing thesis" continues to be hope rather than reality.





Conclusion: What to do, what to do? The most honest thing I can do is to tell you what I personally have done. I've kept my gold coins but I'm out of gold stocks. I've done this on the basis that anything can happen to any stock, but gold is gold, and I hold gold coins for different reasons than I hold gold stocks. The "different reason" is this -- I consider gold as insurance, the ultimate defense against disaster. I can't say that about gold stocks.

LATE NOTES: An awful lot of time is spent in this business trying to predict the end of this bull market (or every other bull market, for that matter). In this endeavor, practitioners use cycles, election spans, point & figure targets, wave formations, astrological signs, and what-have-you.

Sadly, few if any of these techniques prove successful. What I believe is most useful is IDENTIFICATION rather than prediction. A critical item to identify in a bull market is the *psychological phase* that the bull market is in. I'm not going to describe in detail the three phases of a bull market, but suffice it to say that this bull market is obviously in its third phase. The third phase is the speculative, high volume phase, the phase where the public comes in with both feet, the phase where rumors fly and where speculators begin to lose touch with reality.

If you can identify the third or final phase of a bull market (and I have no doubt that we are now in one), then the next task is to identify the area where the market runs out of gas (remember, I said identify, not predict).

First, let's consider the ocean. To identify a change in the ocean's tide, place a stick in the sand as each wave comes in. The stick placed farthest up on the sand identifies the peak or high of the high tide. When the tide turns, your last stick will not be surpassed by incoming waves. Then as the waves continue to roll in, you will note that each successive stick will be placed closer to the ocean. Within an hour or so, you can be sure (based on successive stick placements) that the tide is running out.

By the same token, when the primary trend of the market is in the process of reversing, successive rallies will fail to better the highs. A pattern of lower highs (and lower lows) will form. This tells you that the primary trend is in trouble.

The highs I am watching were listed on page 1, paragraph 3. So let's see if forthcoming rallies can better those record highs. If not, if successive rallies etch out lower tops and bottoms, we will know that the tide is turning. Why guess, why predict, why hope -- let's just try to identify the bear pattern when or as it finally materializes.

Today's wild speculation, today's rising rates, today's torrent of dollars pouring into the funds, tells us that we're in the third phase. It remains for the stock averages to IDENTIFY the actual turn.

Final Notes: Last week the Buying Power on the Lowry's study (page 3) broke to its lowest level since last January. I take this action as very serious and bearish for the market. With the Selling Pressure continuing to rise and with the Buying Power now weakening dramatically, this action tells me that it's simply a matter of time before Selling Pressure overwhelms Buying Power. When that happens, the losses will be building in earnest and a bear market will most probably have started. Timing the crossing? My best guess is that the crossing will occur before the presidential election.

Question: What about the huge inflows of money still coming into the market?

Answer: There's an increasing mass of selling that threatens to overcome those incoming money flows. As losses build up, the incoming money flows will cut back, and then the market will head down for real. Note, by the way, that one billion dollars was recently pulled out of the Magellan Fund. If it can happen to Magellan, it can happen to any or all mutual funds and to the market in general. Note also that despite the huge and continuing influx of cash into the market, the broad S&P has made no visible progress since its February 12 peak, four months ago (S&P up only 1.6% in four months). Finally, note that daily new lows on the NYSE have risen to the 40-60 zone.

BONDS: After their whopping 1996 losses, bonds "may be" ready to correct to the upside. What interested me, however, was watching the bonds rise better than half a point on Friday, June 14, while the stock market (for the first time) *ignored bond strength.* Is the stock market beginning to march to a different drummer?